Supreme Court, U.S.
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No. 01-1424

IN THE

Supreme Court of the United States

JOHN N. BAIN and JOHN G. GILFILLAN, III,

Petitioners,

v.

FREDERICK F. BUECHEL, M.D. and MICHAEL J. PAPPAS, Ph.D., individually and as Trustees of certain Trusts entitled BIOMEDICAL ENGINEERING TRUST,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF APPEALS, STATE OF NEW YORK

BRIEF IN OPPOSITION

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Respondents, Dr. Frederick F. Buechel and Dr. Michael J. Pappas, (collectively, "Respondents"), submit this brief in opposition to the Petition of John N. Bain and John G. Gilfillan, III, (collectively, "Petitioners") which seeks review of a decision of the Court of Appeals of the State of New York in *Buechel v. Bain* ("*Bain*"). 97 N.Y.2d 295, 2001 WL 1636938 (Dec. 20, 2001). The decision by the Court of Appeals does not warrant review by this Court.

PRELIMINARY STATEMENT

The flaw in the Petition for Certiorari is that it focuses on legal abstraction without regard for the facts of the case. The Court of Appeals decision in *Bain* confirmed unanimous decisions in two lower courts holding that Petitioners, New Jersey lawyers, acted fraudulently, in breach of their fiduciary duties, and in violation of applicable Codes of Professional Responsibility, when they induced Respondents to give them an irrevocable interest in a corporation, and, later, in a successor trust, organized to hold a variety of assets created by Respondents, including patents, license agreements, unpatented inventions and royalties. The only consideration for Petitioners' interest in these business ventures was their agreement to render all the necessary legal services for these business ventures on an ongoing, continuing, and perpetual, basis. Thus, under the fee arrangement, Petitioners were required to continually earn their equity interest in Respondents' business ventures by rendering the legal services required by those ventures. However, in violation of applicable legal principles, the fee agreement was improperly structured by Petitioners so as to provide that their equity interest would survive their discharge as counsel and their consequent failure to render any ongoing legal services to the ventures. The New York courts correctly held that this fee arrangement – which would have given Petitioners tens of millions of dollars, without requiring them to render any services in return – was unenforceable, and the courts therefore rescinded Petitioners' interests in Respondents' business.

The issue of the legality of this fee arrangement did not arise under, nor involve, the patent laws of the United States, whether in statutory form or in the form of an ethical code issued by the Patent and Trademark Office (the "PTO Code"), which governs patent practitioners when they are practicing before the Patent Office. More specifically, this case is not governed by, or even related to, the provision in the PTO Code that provides that "in a patent case" a practitioner may "take an interest in the patent as part or all of his or her fee" (App. 155a), the provision on which Petitioners rely for their claim that this case is within the exclusive jurisdiction of the federal courts. This is not a "patent case," as that term is defined in the PTO Code, and the fee arrangement between the parties did not involve "an interest in the patent" for legal services in the Patent Office. For that reason, the New York Court of Appeals properly resolved this case by applying well-established ethical rules and standards governing fee agreements, and related circumstances, in which lawyers enter into business arrangements with their clients.

Moreover, even if the PTO Code had been applicable, the Code does not, as Petitioners contend, conflict with the Court of Appeals decision in any way. To the contrary, the PTO Code includes provisions identical to the ethical provisions in New York and New Jersey applied by the New York courts in this case, which govern a lawyer's ability to enter into a business relationship with his client, the appropriate amount of a legal fee, and the unfettered right of a client to terminate his or her counsel.

Contrary to the Petition, the Court of Appeals did not effectively abolish contingent equity fees for inventors, (Pet. 9) or hold that such fees are "presumptively void." In fact, the Court of Appeals did not even address "contingent equity fees," as such, because this case does not involve a contingent equity fee. What the New York courts did address was a particular type of fee arrangement that ostensibly gave Petitioners a permanent, "*non-contingent*" equity interest in

Respondents' business, an arrangement that far exceeded in scope a single interest in a single patent for completed legal services, the arrangement contemplated by § 10.64(a)(3) of the PTO Code. For that reason, this case also does not pose "problems of federalism of enormous significance to inventors and patent lawyers throughout the country." (Pet. 1) Moreover, the Court of Appeals decision is consistent with provisions in the PTO Code itself, which establish that patent practitioners, like all lawyers nationwide, are prohibited from taking advantage of their clients as Petitioners did in this case – to wit, by inducing their clients to enter into an unfair fee arrangement, which gave the lawyers a permanent, indefeasible equity interest in their clients' business, resulted in an excessive fee for the lawyers, and penalized the clients for exercising their right to terminate their counsel, all without advising their clients of their rights. Thus, this case poses no matters of significance to patent lawyers throughout this country, is not in conflict with the PTO Code, and is not worthy of review by this Court.

Petitioners' independent claim that, in granting summary judgment to Respondents on the basis of collateral estoppel, the Court of Appeals denied them due process of law, is equally without merit and does not warrant review by this Court. Petitioners were not deprived of their opportunity to put forward any defenses they might have had to Respondents' claim for rescission of the unlawful fee agreement. As found by the Court of Appeals, the Appellate Division, and the Supreme Court of New York, Petitioners, who were joined as "essential parties" in the first of the two law suits involved herein, *Rhodes v. Buechel* ("*Rhodes*"), made a tactical decision not to participate in the first action in the hope of getting "two bites of the apple" if their former law partner, R. Gale Rhodes, Jr., lost the first case. They made this strategic choice well aware that the decision in the *Rhodes* action could determine the validity of the fee agreement. Indeed, as the Court of Appeals noted, Petitioners sought a stay of this action, pending the outcome of the *Rhodes* action, because, as they acknowledged, due to "the similarity

of the underlining facts and transactions" in the two actions, "a decision in the *Rhodes* case may estop or bar certain claims in this action." (App. 5a).

The New York courts correctly concluded that Petitioners were bound by the results in *Rhodes* under principles of collateral estoppel, because they were in "privity" with Rhodes as to the issue of the validity of the fee agreement. Rhodes was their law partner at the time the fee arrangement was created, they were co-shareholders with Rhodes in a corporation created to hold Respondents' assets, and, along with Rhodes, they were signatories to, and beneficiaries of, the successor trust at the time the *Rhodes* action was tried. The issues relating to the validity of the business arrangement were vigorously and fully litigated during a lengthy trial in *Rhodes*. Accordingly, the Court of Appeals correctly held that Petitioners were precluded from relitigating the issues already decided in *Rhodes*.

Moreover, after the decision was rendered in *Rhodes*, Petitioners were given the opportunity in this case, on cross-motions for summary judgment, to establish any reasons why they should not be precluded from relitigating the issues decided in *Rhodes*. Petitioners failed to offer any material evidence that might have established any allegedly unique defenses that had not been already decided in *Rhodes*. Therefore, there was no equitable reason to allow them to relitigate the validity of the fee agreement. In short, there is nothing unusual, controversial or questionable about the decisions of the New York courts, at three levels, applying to Petitioners the results in *Rhodes*, and the application of collateral estoppel by the Court of Appeals does not warrant review by this Court.

COUNTER-STATEMENT OF CASE

Choosing to discuss legal abstractions that are irrelevant to this case, Petitioners obscure the nature of the fee arrangement at issue, the procedural history of this case and *Rhodes*, and the bases of the holdings of the New York courts that the fee arrangement was unlawful and in violation of provisions in the Codes of Professional Responsibility applicable in New York,

New Jersey, and the Patent Office, as well, governing business transactions between attorneys and clients, the appropriate amount of fees, and the clients' right to terminate counsel. To bring this case from the abstract to the concrete, we begin with a summary of the relevant facts and procedural history of this and the *Rhodes* action.

The Inception of the Parties' Relationship and the Fee Arrangement

In 1974, Respondents, internationally known inventors of prosthetic joint implants, entered into an oral agreement with Petitioners' law firm, Bain, Gilfillan & Rhodes, pursuant to which the firm was to render legal services to Respondents in connection with the preparation and prosecution of a patent application on a prosthetic device Respondents had developed. (App. 1a, 78a-79a) In return, the law firm, which at that time was comprised of only three lawyers – Petitioners and Rhodes – was to receive a one-third interest in any income Respondents might receive in connection with that single invention. (App. 2a, 78a-79a) Less than one year later, in July 1975, in order to entrench the firm's relationship with Respondents, Petitioners and Rhodes induced Respondents to form a corporation, Biomedical Engineering Corporation ("BEC"), to exploit any of their future inventions and collect royalties on the sale of such inventions. (App. 2a, 81a-82a) Petitioners and Rhodes were given, collectively, one-third of the stock of the corporation in return for their agreement to render continuing and future legal services to the corporation, an agreement that the lawyers failed to memorialize in writing. (App. 2a, 81a-82a)

Over the course of the next seven years, Bain, Gilfillan & Rhodes performed routine legal services for BEC, the great majority of which were performed by Rhodes himself. (App. 87a) In 1981, Rhodes withdrew from the firm because of a dispute with Petitioners. (App. 2a) At about the same time, Respondents learned that the firm's earlier advice that they incorporate their business venture exposed them to unnecessary taxes on royalty income they might receive from the successful

licensing of their inventions. (App.88a-89a) Therefore, to address Rhodes' departure from the firm, and the tax problems as well, the technology created by Respondents was transferred from BEC into two trusts that replaced BEC as the vehicles for conducting Respondents' business. (App. 2a) Petitioners and Rhodes became beneficiaries of one of the trusts, Biomedical Engineering Trust (the "Trust"), and were each granted a one-ninth beneficial interest in the Trust in exchange for their agreement to render legal services to the Trust. (*Id.*) Due to the dissolution of Bain, Gilfillan & Rhodes, only Petitioners were required to continue rendering legal services on an on-going basis to the Trust.[1] (App. 90a) Significantly, the trust agreement provided that Petitioners' beneficial interests in the Trust could not be extinguished, even if they ceased providing such legal services. (App. 92a, 101a-103a)

The *Rhodes* Action and Petitioners' Role In It

In 1987, a dispute erupted between Rhodes and Respondents concerning the allocation of royalty payments to the trusts, and Rhodes commenced a lawsuit seeking to remove Respondents as trustees and for monetary relief. (App. 3a) Early in the litigation, Rhodes joined Petitioners as "necessary parties" to the action, since they, along with him, were beneficiaries of the Trust, and might be affected by the relief he sought. (App. 3a) Thereafter, in 1991, Respondents asserted counterclaims against Rhodes, who had created the fee arrangement on behalf of his firm, challenging the ethical validity of Rhodes' interest in the trusts created to hold Respondents' assets (the "Ethics Counterclaims"). (App. 3a) As the Court of Appeals explained:

> [Respondents] asserted counterclaims against Rhodes for breach of fiduciary duty and malpractice, alleging among other things that "the agreements were unfair" and that Rhodes, "while acting as their attorney induced [Respondents] to enter into the

1. Rhodes became a beneficiary of a separate trust, Biomedical Engineering Trust II, for which he alone agreed to provide the necessary on-going legal services. (App. 91a)

> unfair agreements by taking unfair advantage of his fiduciary capacity and superior knowledge, by deceiving [Respondents] as to the value of his and/or the law firm's services and by failing to disclose . . . the value of the one-third interest relinquished by the inventors."

(App. 3a)

As parties in *Rhodes*, Petitioners were on notice of the Ethics Counterclaims and their potential to nullify their interests, as well as Rhodes', in the Trusts. (App. 3a-4a, 67a) As the Court of Appeals found, Petitioners expressly acknowledged this potentiality during the pendency of the *Rhodes* action:

> Recognizing their unity with Rhodes in regard to the validity of the challenged fee arrangement, on March 12, 1992, Bain wrote [Respondents] that he was unclear as to how the counterclaims could be narrowly construed solely against Rhodes. Bain wrote that he and Gilfillan were "concerned that the counterclaims could be interpreted broadly to assert overreaching either by the law firms in which Rhodes, Gilfillan and I were involved or, at the least by Rhodes as a partner or agent of those law firms, thereby potentially extending the consequences of the alleged wrongdoing by Rhodes to Gilfillan and myself."

(App. 3a-4a) Despite the fact that Petitioners were "parties to the *Rhodes* action with notice of the issues to be decided in that case," (App. 11a), and despite Petitioners' explicit acknowledgement that the counterclaims in *Rhodes* could be construed to encompass their conduct, Petitioners, experienced lawyers, knowingly chose not to actively participate in the *Rhodes* action.[2]

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2. However, Petitioners did, albeit selectively, participate in discovery in *Rhodes*. They "produced documents for the litigation, received copies of select documents used in the trial, (including deposition transcripts), and agreed to testify as witnesses on behalf of Rhodes before changing their minds at the last minute." (App. 12a)

In 1995, the relationship between Petitioners and Respondents became strained due to a number of disputes, including Petitioners' failure to provide competent legal services to Respondents, which resulted in the loss of certain valuable patent rights. As a result, Respondents discharged Petitioners in January 1995 and sought to amend their claims in the *Rhodes* action to assert affirmative relief against Petitioners. However, that motion was denied on the grounds that it would unduly delay the trial in *Rhodes*. (App. 4a)

The *Rhodes* Trial

The *Rhodes* action was tried in 1995. The trial involved over 5,000 pages of testimony, and hundreds of exhibits, including testimony by Professor Geoffrey C. Hazard, Jr., then Director of the American Law Institute and one of the country's leading authorities on legal ethics, and three New Jersey ethics experts, including two called by Rhodes. (App. 46a) Although the trust agreements provided that New York law was applicable to the dispute, since Rhodes and Petitioners were New Jersey lawyers, the ethics experts testified about the legal and ethical requirements of the Codes of Professional Responsibility in New Jersey and New York. In addition, the trial court heard testimony from Respondents, Rhodes and others, concerning the circumstances leading to the original 1974 fee agreement, the creation of BEC in 1975, the establishment of the trusts in 1983, and all the other relevant facts. Shortly before the trial, Petitioners entered into a "joint defense" agreement with Rhodes, and agreed to testify on Rhodes' behalf. However, during the trial, they changed their tactics and refused to appear at the last moment. (App. 12a)

In short, Rhodes, who had many millions of dollars at stake and was represented by experienced counsel, vigorously litigated the validity of the fee agreement and sought its full enforcement.[3]

3. Among other things, the trial court received in evidence an opinion by the New York City Bar Association (Ethics Opinion 80-14 (1980)) which expressly recognized that patent lawyers may receive a one-third contingent interest in their clients' patents in return for past

(Cont'd)

The Decision in *Rhodes*

In March, 1998, the Supreme Court of New York issued a lengthy decision in *Rhodes* which contained detailed findings of fact and conclusions of law regarding the propriety of the fee arrangement. (App. 75a-118a) The Supreme Court expressly found that the fee arrangement was far more than a "proprietary interest in certain patents as the fee for prosecuting those patents on behalf of Respondents," as the Petitioners have characterized it. (Pet. 1) Rather, the *Rhodes* court held:

> Rhodes had converted his [firm's] attorney fee which was a one-third interest in a single invention into a *one third equity interest in a corporation* responsible for the exploitation of all [the clients'] future inventions.

(App. 102a) (emphasis added) In exchange for that equity interest in a corporation, whose assets were later transferred to two trusts, Rhodes and Petitioners agreed to provide all the necessary continuing and future legal services to the parties' venture. These services included – or at least were intended to include – the prosecution and defense of patent infringement actions, the negotiation of licensing agreements, and the other legal services necessary to protect and preserve Respondents' intellectual property. (App. 78a, 80a, 87a) However, the *Rhodes* court expressly found that, in connection with this arrangement, the lawyers did not properly advise Respondents of their rights. Specifically, they did not advise Respondents that, by granting their attorneys an irrevocable interest in their business, they were abridging their clients' right to freely terminate their counsel and extinguish their equity interest, which is a violation of the rule against non-refundable retainers. (App. 102a-103a) (*See In re Cooperman*, 633 N.E.2d 1069 (N.Y. 1994); *Cohen v.*

(Cont'd)
legal services, so long as relevant disclosures are made and the interest does not create an excessive legal fee. This ethics opinion is identical in substance to inter-related provisions in the PTO Code of which Petitioners have made so much.

Radio Electronics Officers Union, Dist.3, 645 A.2d 1248 (N.J. Super. Ct. App. Div. 1994), *modified*, 679 A.2d 1188 (N.J. 1996)). Moreover, neither Petitioners nor Rhodes disclosed the conflicts of interest involved when attorneys go into business with their clients or advised the clients to consult with independent counsel regarding the propriety of the business arrangement. (App. 80a, 81a,82a-83a, 102a-103a.) Due to these many ethical violations, the court held that the fee arrangement was the product of fraud, overreaching, breach of fiduciary duty, and violated the Code of Professional Responsibility. (App. 97a-110a, 114a.) As a result, the court rescinded, *ab initio*, Rhodes' beneficial interest in the trusts. (*Id.* at 118a, 119a-122a.)

The *Rhodes* decision was unanimously affirmed by the New York Appellate Division, 685 N.Y.S.2d 65 (App. Div. 1999), and leave to appeal was denied by the New York Court of Appeals. 711 N.E.2d 984 (N.Y. 1999).

The Present Action Against Petitioners

In March 1995, before the trial in *Rhodes* began, Respondents commenced a separate action against Petitioners in the New York courts (the "*Bain* action"), in which they sought a judgment rescinding Petitioners' interests in the Trust on the same grounds on which they were seeking to rescind Rhodes' interest. In stark contrast to the position Petitioners have taken before this Court, Petitioners responded by moving to stay the action pending the decision in *Rhodes* on the ground that:

> Because of the similarity of the underlying facts and transactions in both the *Rhodes* action and this one, proceeding with this action at this time would be duplicative and a waste of judicial resources. *Indeed, a decision in the Rhodes case may estop or bar certain claims in this action.*

(App. 5a) (emphasis added). Petitioners' application for a stay was granted, and this case was held in abeyance for three years awaiting the decision in *Rhodes*. The stay was lifted when the Supreme Court rendered its decision in *Rhodes*. (App. 6a)

Respondents then moved for partial summary judgment seeking to rescind Petitioners' interests in the Trust based on the findings in *Rhodes* that the lawyers' interests in the Trust had been obtained through fraud, overreaching, and breaches of the Code of Professional Responsibility. On May 26, 1999, the New York Supreme Court ordered that Petitioners' interests in the Trust, like Rhodes', be rescinded, *ab initio*, and directed Petitioners to return $6.8 million (plus interest) that they had received from the Trust pursuant to the illegal fee agreement, (less the amount of a proper legal fee to be determined on the basis of *quantum meruit*). (App. 56a-59a, 65a-71a) The New York Appellate Division unanimously affirmed the summary judgment ruling, 713 N.Y.S.2d 332 (App. Div. 2000) (App. 40a-55a), and, thereafter, the Court of Appeals affirmed, 97 N.Y.2d 295 (2001) (App. 1a-39a)

Each of the New York courts rejected Petitioners' argument that they had been denied their opportunity to litigate the issue of the enforceability of the fee agreement. The Court of Appeals held, pursuant to the doctrine of collateral estoppel, that "[Petitioners] are barred from now once again litigating the validity of a trust agreement that was – after extensive pretrial and trial proceedings involving them – found to be invalid." (App. 9a) The Court of Appeals explained that the doctrine of collateral estoppel "is a flexible one," which requires a "case-by-case analysis of the facts and realities." (App. 9a) The Court further explained that:

> In the end, the fundamental inquiry is whether relitigation should be permitted in a particular case in light of . . . fairness to the parties, conservation of the resources of the court and the litigants, and the societal interests in consistent and accurate results. No rigid rules are possible, because even these factors may vary in relative importance depending on the nature of the proceedings . . . (*see, Staatsburg Water Co. v. Staatsburg Fire Dist.*, 72 N.Y.2d 147, 153, [1988] [citations omitted]).

(App. 9a)

Based on a fact intensive analysis, the Court of Appeals held that Petitioners were bound by the decision in *Rhodes* because, among other reasons, they were in privity with Rhodes. This determination of privity was based on

> a confluence of factors . . . including [Petitioners'] relationship with Rhodes vis-à-vis the fee arrangements, their involvement in the action, their awareness of issues that would be decided, and their acknowledged tactical decisions regarding the *Rhodes* litigation.

(App. 13a, n.*)

Petitioners' role as parties in the *Rhodes* action was an important factor in the Court of Appeals decision. The Court emphasized that since Petitioners were "parties to the *Rhodes* action with notice of the issues to be decided in that case," (App. 11a), and, indeed, had acknowledged the potential preclusive effect of that decision on their rights:

> as a policy matter, . . . a "party to a lawsuit cannot sit by idly while a contract, to which he is also a party, is judicially construed without being precluded by the result." . . . Knowing that the validity of the trust was being vigorously contested in *Rhodes*, and knowing the potential serious adverse consequences of the litigation, in this particular case it is appropriate to deem [Petitioners'] interests represented by Rhodes. [Petitioners] cannot be rewarded for their conscious tactical decision not to take a more active role in that litigation by now allowing the very same issues and facts to be relitigated. A contrary determination would undermine a policy interest that is at the heart of collateral estoppel — discouraging relitigation of issues and the potential for inconsistent outcomes.

(*Id.*) (internal citation omitted).

Petitioners' Unsuccessful Effort to Challenge the Subject Matter Jurisdiction of the New York Courts

After the New York court granted summary judgment to Respondents in this action, and nearly *eight years* after the issue of the propriety of the fee agreement was first raised in the *Rhodes* action, Petitioners first put forth their theory that the state courts lacked subject matter jurisdiction over both the fully completed *Rhodes* action and this case. Specifically, Petitioners moved to dismiss this action for lack of subject matter jurisdiction, claiming that applicable state law was entirely preempted by a single provision in a multi-provision ethics code applicable only to patent lawyers and practitioners in cases before the Patent Office. That provision, § 10.64(a)(3), provides that "in a patent case [a practitioner may] take an interest in the patent as part or all of his fee." (App. 155a)

The Supreme Court, the Appellate Division, and the Court of Appeals each decisively rejected Petitioners' jurisdictional argument. (App. 13a-14a, 53a, 60a-64a) As the Court of Appeals found:

> This case is not preempted by patent law because [Petitioners], the inventors, did not plead any substantive questions of patent law as an element of the claims asserted against defendants. A case arises under patent law "when a well-pleaded complaint establishes either that federal patent law creates the causes of action or that [Petitioners'] right to relief necessarily depends on resolution of a substantial question of federal patent law, in that patent law is a necessary element of one of the well-pleaded claims." . . . Further, Federal patent statutes do not preempt State law in this case . . . Nor do lower court decisions invalidate a patent attorney's right to receive an interest in a client's patent as full or partial payment.
>
> Rather, this case addresses the necessary disclosures attorneys must make and the ethical obligations they

> must maintain in the course of their interaction with clients. Although Federal patent law recognizes that attorneys may receive an interest in patents in lieu of traditional fee arrangements, the need for disclosure mandated by the Code of Professional Responsibility governing the practice of law in this State is not obviated.

(App. 14a) (internal citations omitted)

REASONS FOR DENYING THE WRIT

I. THE NEW YORK COURTS PROPERLY EXERCISED JURISDICTION AND HELD THE FEE ARRANGEMENT UNENFORCEABLE

The Court of Appeals correctly rejected Petitioners' argument that the PTO Code, which (a) only applies to patent lawyers and practitioners when they are practicing before the Patent Office, and (b) is no different in substance from relevant ethical rules applicable in New Jersey, New York and other states, divested the New York state courts of jurisdiction to determine the enforceability of the fee arrangement between the parties. Leaving aside the fact that this is not "a patent case" before the Patent Office, the provision on which Petitioners rely simply does not apply to the issue of the illegality of the business arrangement at bar. This arrangement gave Petitioners an equity interest in a business venture, for which Petitioners were to render continuing legal services. It did not simply involve an interest in a patent received as a fee for completed services in a "patent case." The issue of the propriety of the fee agreement raised state law questions concerning the circumstances in which attorneys may go into business with their clients. Therefore, because the resolution of this issue did not "necessarily depend[] on . . . a substantial question of federal patent law," *Christianson v. Colt Inds. Operating Corp.*, 486 U.S. 800, 808-09 (1988), it does not provide a basis for exclusive federal jurisdiction.

This case also does not implicate the Supremacy Clause because the Court of Appeals decision does not "conflict with federal law and public policy," nor does it "encumber the federal standard, [as reflected in the PTO Code] to the point of eradicating it in practice." (Pet. 11, 12) To the contrary, the PTO Code, which expressly provides that it does not preempt state law (37 C.F.R. § 10.1), is identical to the ethical standards applied by the Court of Appeals governing business relationships between attorneys and their clients, and related circumstances.

Finally, Petitioners' contention that this case "arises under" the federal patent laws also was properly rejected by the New York courts, because, like Petitioners' other arguments, it is premised on the erroneous contention that the fee agreement in this case is governed by § 10.64(a)(3) of the PTO Code.

A. Section 10.64(a)(3) of the Patent Code Is Not Applicable to this Action

Petitioners' argument that the Court of Appeals decision violates the Supremacy Clause, and that this case "arises under" the federal patent laws, is based on the erroneous assumption that § 10.64(a)(3) of the PTO Code governs this case to the exclusion of all other legal and ethical standards. The argument collapses upon examination of the parties' fee arrangement, which concerns neither the acquisition of an equity interest in a patent as a fee, the arrangement contemplated by § 10.64(a)(3) of the PTO Code, nor "a patent case," as that term is used in the PTO Code.

The decisions of the New York State courts establish that the action involves the validity of a legal fee in the form of a long-term business arrangement, which was, at all material times, that of a joint business venture for which the lawyers were to provide legal services. (App. 80a, 102a-103a) The venture originally took the form of a corporation, in which the lawyers held one-third of the stock in return for their performance of a variety of legal services. (App. 2a, 81a, 82a) Through fraudulent misrepresentations, the lawyers induced their clients to assign all their inventions and other assets to

that corporation. (App. 83a) Later, the parties' interests in the corporation were converted into interests in a business trust that purportedly would survive the lawyers' discharge as counsel. (App. 2a, 89a-91a, 105a-109a) As the New York courts properly found in *Rhodes*, Petitioners entered into this long term business venture with Respondents without adequate disclosure to them of the conflicts of interest involved, without advising the clients to seek the advice of independent counsel, without advising the clients of their unfettered right to terminate the attorneys and thereby extinguish their equity interests in Respondents' business, and through other fraudulent means. (App. 5a-6a, 80a-82a) For these reasons, the *Rhodes* court properly held that the fee arrangement – which was wholly different in nature from a single contingent equity fee for completed services – was unenforceable as a matter of law. (*See* App. 97a-105a, 109a-110a.)

In addition, the scope of Petitioners' representation of Respondents was by no means limited to practice involving "a patent case" before the Patent Office. The PTO Code expressly provides that a "patent case" is limited to the "preparation and prosecution of applications for patent[s]." *See* 37 C.F.R. §10.5 *et seq.* Here, Petitioners agreed to provide broad-based legal services to defendants, services that included – or at least were intended to include – the prosecution and defense of patent infringement actions, the negotiation of licensing agreements, and the other legal services necessary to protect and preserve defendants' intellectual property. (App. 78a, 80a, 87a) For these reasons, section 10.64(a)(3) of the PTO Code is not applicable to, much less determinative of, this action.

B. The Court of Appeals Decision Does Not Violate the Supremacy Clause Because the PTO Code Does Not Preempt State Law

Petitioners' argument that the Court of Appeals decision violates the Supremacy Clause should be rejected for the independent reason that it is based on the erroneous premise that the Court of Appeals decision "conflict[s] with federal law

and public policy" as found in the PTO Code. (Pet. 12) The PTO Code imposes ethical constraints on an attorney's arrangements with his or her client that are identical to those imposed in this case and in *Rhodes* by the New York courts. The PTO Code does not preclude inventors, such as Respondents, who have entered into an unethical or fraudulent fee agreement with patent attorneys, from suing in state court to determine their rights, or to recover for fraud, malpractice, misrepresentations, or breaches of fiduciary duty.[4] The very code on which Petitioners rely expressly declares that it does *not* preempt state law:

> This part governs solely the practice of patent, trademark, and other law before the Patent and Trademark Office. *Nothing in this part shall be construed to preempt the authority of each State to regulate the practice of law* except to the extent necessary for the Patent and Trademark Office to accomplish its Federal objectives.

37 C.F.R. § 10.1. (emphasis added)

Petitioners nevertheless contend that the PTO Code *implicitly* preempts state law, because the regulation of patent practitioners is a "general field occupied by federal law" and "the New York rules eviscerate the federal rules for all practical purposes." (Pet. 13) Petitioners are wrong in both respects.

To infer preemption of state law, a court must conclude either that: (1) Congress or a federal agency "intends that federal law occupy a given field," *California v. ARC America Corp.*, 490 U.S. 93, 100-01 (1989); or (2) the state law "actually conflicts with federal law, that is, when compliance with both federal and state law is impossible, or when the state law stands as an obstacle to the accomplishment and

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4. Petitioners concede that, as patent lawyers, who are members of the bars of New Jersey and other states, they must comply with the ethical standards applicable in those states, in addition to the ethical standards governing practice before the Patent Office. (Pet. 15, n.10) *See Kroll v. Finnerty*, 242 F.3d 1359, 1365 (Fed. Cir. 2001).

execution of the full purposes and objectives of Congress[.]" *Id.* (quotations omitted).[5]

The first criterion is not met because the Patent Office did not intend that the PTO Code "occupy the field" of regulation of patent lawyers and practitioners. As noted above, the PTO Code expressly provides that it was not intended to preempt state law. 37 C.F.R. § 10.1[6] Indeed, the Code explicitly

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5. The New York courts correctly held that Petitioners had not overcome the presumption that federal law is not intended to supersede state law regulatory schemes. *See, e.g., Environmental Encapsulating Corp. v. City of New York*, 855 F.2d 48, 58 (2d Cir. 1988). That burden is particularly high in cases that rely on the notion of an implied preemption and concern a federal regulatory scheme that involves the state's historic police powers (*e.g.*, the state's power to regulate attorneys it has admitted to practice before its courts). *See, e.g., Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. Abrams*, 899 F.2d 1315, 1319 (2d Cir. 1990), *cert. denied*, 499 U.S. 912 (1991)

> When Congress legislates in a field traditionally occupied by the States, "we start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress." . . . Thus, a litigant challenging a state statute on preemption grounds in such a field must overcome "a presumption against finding preemption of state law."

(*quoting California v. ARC America Corp.*, 490 U.S. 93, 102 (1989) and *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947)); *see also Medtronic, Inc. v. Lohr*, 518 U.S. 470, 485 (1996).

6. The Patent Office explained in its Notice of Proposed Rulemaking that the preamble to the PTO Code, 37 C.F.R. § 10.1, was proposed in light of this Court's decision in *Sperry v. State of Florida ex rel. Florida Bar*, 373 U.S. 379, 402 (1963), and to make it

> clear the PTO's intent to limit Subpart 10 solely to the practice of patent, trademark, and other law before the PTO . . . [and] to indicate that Subpart 10 shall *not* be construed to preempt the authority of any State to maintain control over the practice of law within its borders, *except* to the extent necessary for the PTO to accomplish its federal

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contemplates concurrent supervisory oversight. It requires that notification be given by those patent attorneys who have been disciplined or suspended by the PTO to "all bars of which he or she is a member." *See* 37 C.F.R. § 10.158(b)(1); 37 C.F.R. § 10.159. The PTO Code's requirement that the appropriate state disciplinary authorities be given notice of a patent attorney's misconduct makes manifestly clear that the Patent Office envisioned concurrent disciplinary jurisdiction between the Patent Office and the states.

The second criterion – that preemption can be implied when state law conflicts with federal law – also is not met. The PTO Code's acknowledgment that a patent lawyer may acquire an interest in a patent is limited by the various other provisions in the PTO Code that govern business transactions between attorneys and clients, the appropriate amount of fees, and the client's right to terminate counsel. Thus, the PTO Code provides that:

> A practitioner shall not enter into a business transaction with a client if they have differing interests therein and if the client expects the practitioner to exercise professional judgment therein for the protection of the client, unless the client has consented after full disclosure.

37 C.F.R. § 10.65. This provision is *identical* to the ethical rules imposed by the disciplinary codes of both New York and New Jersey that were the basis on which *Rhodes* and *Bain* were decided, thus destroying any notion of a conflict between the

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> objectives. These changes are being made to make clear that the PTO intends to regulate only conduct related or relevant to the practice of law before the PTO.

Practice Before the Patent and Trademark Office, Notice of Proposed Rulemaking, 49 Fed. Reg. 33,790, (August 24, 1984) (emphasis in original). *See also* Rules and Regulations, Department of Commerce, Practice Before the Patent And Trademark Office, 50 Fed. Reg. 5158, 1985 WL 90221, *5158 (February 6, 1985).

state laws and ethical rules governing this dispute and the PTO Code. *Cf.* 22 N.Y.C.R.R. § 1200.23(a); N.J.R.P.C. § 1.8(a). The PTO Code, like the ethical rules of New York and New Jersey, also prohibits a patent practitioner from collecting an excessive fee. *See* 37 C.F.R. § 10.36(a); *Cf.* 22 N.Y.C.R.R. § 1200.11(a); N.J.R.P.C. § 1.5(a), or from abridging a client's unfettered right to discharge their counsel. 37 C.F.R. § 10.40(a); *Cf.* 22 N.Y.C.R.R. § 1200.15(a)(3); N.J.R.P.C. § 1:16(a)(3).

Further, section 10.64 of the PTO Code merely codified what has long been permitted in New York, New Jersey and elsewhere. *See* Association of the Bar of the City of New York Ethics Opinion 80-14 (1980) (a lawyer may take an interest in a patent as a fee, but it may be subject to limitations on entering into a business arrangement with a client and rules against excessive fees). As noted by the PTO:

> Proposed § 10.64(a)(3) is now consistent with Informal Opinion No. 280 of the American Bar Association which states: "A lawyer may acquire an interest in a patent for his [or her] fee."

49 Fed. Reg. at 33798. Thus, rather than being in *conflict*, the PTO Code provision on which Petitioners entirely rely is in complete conformity with the state laws and principles on which *Rhodes* and *Bain* were decided.

The absence of any conflict between the PTO Code and the applicable state ethical codes and standards renders *Sperry v. State of Florida ex rel. Florida Bar*, 373 U.S. 379 (1963), and *Silverman v. State Bar of Texas*, 405 F.2d 410 (5th Cir. 1968), inapposite. In *Sperry* and *Silverman*, there were direct conflicts between the state law at issue and the patent regulations.[7]

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7. *Sperry*, for example, held that a praetitioner who limited his practice to patent work before the Patent Office was not required to be admitted to practice law in the state because the Patent Office explicitly permitted non-lawyers to practice before it. 373 U.S. at 382-83, 404. In *Silverman*, the court merely held that a state bar rule prohibiting a patent attorney from holding himself out as such conflicted with patent regulations explicitly permitting such advertisements. 405 F.2d at 414-15.

In this case, by contrast, the principles applied by the New York courts, requiring full disclosure by attorneys entering into business relationships with their clients, and precluding excessive fees and non-refundable retainers, are entirely consistent with the PTO Code.

The Federal Circuit Court of Appeals recent decision in *Kroll v. Finnerty*, 242 F.3d 1359 (Fed. Cir. 2001), is instructive. The *Kroll* court rejected the identical argument made by Petitioners that the PTO Code vests federal courts with exclusive jurisdiction to supervise a patent attorney's misconduct, and held that the New York bar was free to discipline the plaintiff, who, like Petitioners, was a member of both the federal patent bar and a state bar. 242 F.3d at 1364-65. In *Kroll*, as here, it was "beyond serious argument to suggest that [the] state action would frustrate the ability of the PTO to accomplish its federal objectives." Indeed, the court held that "by disciplining patent attorneys, who violate their ethical duties to clients, the [state disciplinary committee], would advance the goals of the patent laws by promoting better relationships between patent lawyers and their clients." *Id.* at 1365. Similarly, the decision of the Court of Appeals furthers the express objectives of the PTO Code, which preclude patent lawyers from entering into unfair business ventures with their clients, without their clients' informed consent.

In summary, there is no merit in Petitioners' contention that the New York decisions "circumscribe federally authorized patent lawyers from practicing patent law within their borders, including limiting the right to accept equity fees authorized by 37 C.F.R.§ 10.64." (Pet. 14) Rather, the Court of Appeals decision is entirely consistent with the PTO Code, and this Court's decision in *Sperry*.

C. This Case Does Not Arise Under the Patent Laws

Petitioners argue that this case vests the federal courts with exclusive jurisdiction pursuant to 28 U.S.C. § 1338(a)[8] because

8. Section 1338(a) provides, in relevant part: "The district courts shall have original jurisdiction of any civil action arising under any Act of Congress relating to patents. . . ."

"the proper disposition of Respondents' claim, can only be determined by reference to applicable federal patent regulations, which expressly authorize patent practitioners to accept an equity interest in a patent as part or all of their fee." (Pet. 11) (citations omitted) However, since, as shown above, Petitioners' preemption argument is "'so attenuated and unsubstantial as to be absolutely devoid of merit,'" there is no basis for jurisdiction arising under the federal patent law. *Kroll*, 242 F.3d at 1366 (*quoting Hagans v. Lavine*, 415 U.S. 528, 536-37 (1974)).[9]

Moreover, while Petitioners argue that the Court of Appeals applied an "overly restrictive formulation" of the scope of 28 U.S.C. § 1338(a), they fail to cite one case in which the court held that there was exclusive federal patent jurisdiction over an issue concerning the enforceability of an agreement relating to the ownership of patents (among the other types of intellectual property assets held in the Trust). Nearly a century of case law makes it clear that disputes, which involve questions of ownership of patents, do not "arise under" the patent laws and fall within the jurisdiction of the federal courts:

> the question of who owns the patent rights and on what terms typically is a question *exclusively for state courts*. . . . [T]hat long has been the law. It is well-settled that if the patentee pleads a cause of action based on rights created by a contract, or on the common law of torts, the case is not one 'arising under' the patent laws.

Jim Arnold Corp. v. Hydrotech Systems Inc., 109 F.3d 1567, 1572 (Fed. Cir.), *cert. denied sub nom., Baker Hughes, Inc. v. Jim Arnold Corp.*, 522 U.S. 933 (1997) (emphasis added) (and cases cited therein).[10]

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9. *See also Hunter Douglas, Inc. v. Harmonic Design, Inc.*, 153 F.3d 1318, 1328 (Fed. Cir. 1998), *cert. denied*, 525 U.S. 1143 (1999) ("'wholly insubstantial and frivolous' claims do not merit federal jurisdiction") (quoting *Bell v. Hood*, 327 U.S. 678, 682-83 (1946)).

10. The cases Petitioners have cited are not to the contrary, because, unlike here, those cases did raise issues *requiring* the application of the

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Since the issue of the legality of Petitioners' equity interest in Respondents' business does not implicate, let alone "necessarily depend on," "a substantial question of federal patent law," *Christianson*, 486 U.S. at 808-09, there is no basis to review the Court of Appeals decision on the issue of subject matter jurisdiction.

II. THE NEW YORK COURTS CORRECTLY PRECLUDED PETITIONERS FROM RE-LITIGATING THE ISSUE OF THE ENFORCE-ABILITY OF THE FEE AGREEMENT

Petitioners contend that they were denied due process when the New York courts applied to them findings of fact and conclusions of law made in *Rhodes*, and they argue that the Court of Appeals "applied preclusion principles offensively to estop Petitioners from mounting any defense whatsoever to the claims asserted against them." (Pet. 2) This Court long ago held that the due process clause requires "notice and opportunity for hearing appropriate to the nature of the case." *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306, 313 (1950). However, "there is involved in [the due process clause] no right to litigate

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federal patent law. The cases either required the resolution of a patent infringement issue – *see 3D Sys., Inc. v. Aarotech Labs, Inc.*, 160 F.3d 1373 (Fed. Cir. 1998); *Scherbatskoy v. Halliburton Co.*, 125 F.3d 288 (5th Cir. 1997); *Alco Standard Corp. v. Tennessee Valley Authority*, 808 F.2d 1490,1494 (Fed. Cir. 1986), *cert. dismissed*, 483 U.S. 1052 (1987) – the validity and enforceability of a patent – *Hunter Douglas, Inc., supra.*, 153 F.3d at 1330 – the PTO's exercise of its administrative authority to issue patents, or vest title in a patent to the United States, rather than the inventor – *see Morganroth v. Quigg*, 885 F.2d 843 (Fed. Cir. 1989); *Cedars-Sinai Medical Center v. Watkins*, 11 F.3d 1573 (Fed. Cir. 1993); *Dubost v. United States Patent & Trademark Office*, 777 F.2d 1561 (Fed. Cir. 1985) – or the review of a determination by the PTO that a particular attorney was ineligible to practice before it – *see Franchi v. Manbeck*, 972 F.2d 1283 (Fed. Cir. 1992); *Jaskiewicz v. Mossinghoff*, 802 F.2d 532 (D.C. Cir. 1986); *Wyden v. Commissioner of Patents & Trademarks*, 807 F.2d 934 (Fed. Cir. 1986).

the same question twice." *Baldwin v. Iowa State Traveling Men's Ass'n.*, 283 U.S. 522, 524 (1931).

Petitioners were not deprived of their due process rights in this case because they, in fact, had two opportunities to challenge Respondents' claims that the fee arrangement was illegal and unenforceable, first in the *Rhodes* case, in which they were named as "essential parties" and in privity with Rhodes, and then in this case. It was for those reasons that the Court of Appeals properly held, under the equitable doctrine of collateral estoppel, that, having been *both* parties in the first action *and* in privity with Rhodes, Respondents were precluded from relitigating the issues resolved in *Rhodes*.

A. Petitioners Were Properly Bound by The Decision in *Rhodes* by Virtue of Having Been Parties to that Action.

This Court has explained that:

> [a] fundamental precept of common-law adjudication, embodied in the related doctrines of collateral estoppel and *res judicata*, is that a "right, question or fact distinctly put in issue and directly determined by a court of competent jurisdiction . . . cannot be disputed in a subsequent suit between the same parties or their privies."

Montana v. United States, 440 U.S. 147, 153 (1979) (quoting *Southern Pacific R. Co. v. United States*, 168 U.S. 1, 48-49 (1897)). "Collateral estoppel . . . has the dual purpose of protecting litigants from the burden of relitigating an identical issue with the same party or his privy and of promoting judicial economy by preventing needless litigation." *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 326 (1979). *See also Montana*, 440 U.S. 153-54 ("To preclude parties from contesting matters that they have had a full and fair opportunity to litigate protects their adversaries from the expense and vexation attending multiple lawsuits, conserves judicial resources and fosters reliance on judicial action by minimizing the possibility of inconsistent decisions.")

The doctrine of collateral estoppel under New York law is identical to the doctrine as defined by this Court. It "precludes a party from relitigating in a subsequent action or proceeding an issue raised in a prior action or proceeding and decided against that *party or those in privity*." *Ryan v. New York Tel. Co.*, 467 N.E.2d 487, 490 (N.Y. 1984) (emphasis added). *Cf. Richards v. Jefferson Cty.*, 517 U.S. 793, 797-98 (1996); *Montana*, 440 U.S. at 153. Since Petitioners were parties in *Rhodes*, with actual notice that Respondents were challenging the legality of the lawyers' fee arrangement with Respondents in its entirety, *a fortiori*, they are bound by the findings in *Rhodes* under both New York and federal law.

Moreover, as the Court of Appeals observed, collateral estoppel is an equitable doctrine "grounded in the facts and realities of a particular litigation." (App. 8a, 9a) (*citing Staatsburg Water Co. v. Staatsburg Fire Dist.*, 572 N.E.2d 754 (1988)). As parties in *Rhodes*, Petitioners were well aware of the proceedings therein, but engaged in a tactical gambit whereby they would take advantage of any decision upholding the fee agreement, but seek to avoid the decision, and get a "second bite at the apple," if the decision were adverse. (App. 11a, 13a; *see also* 53a, 68a). The record is clear that Petitioners knew that the decision in *Rhodes* might determine their own rights with respect to their fee agreement, and that they could be bound by the result in *Rhodes*. Indeed, they sought a stay of this lawsuit pending the decision in *Rhodes* based on their own argument that "a decision in the *Rhodes* case may estop or bar certain claims in this action." (App. 5a) It was only *after* the *Rhodes* court found that the fee agreement was unenforceable, that Petitioners claimed that the findings in *Rhodes* should not be applied in this action. It was based on these facts that the Court of Appeals concluded:

> [I]t is appropriate to deem [Petitioners'] interests represented by Rhodes. [Petitioners] cannot be rewarded for their conscious, tactical decision not to take a more active role in that litigation by now

> allowing the very same issues and facts to be relitigated.

(App. 11a)

The decision before the *Rhodes* trial denying a motion by Respondents to amend their pleading to assert specific claims for damages and equitable relief against Petitioners does not alter this result. Petitioners erroneously contend that this decision "freed [them] of liability." (Pet. 29) However, as the Court of Appeals properly held: "All that denial of the motion to amend guaranteed was that [Petitioners] would not be subject to a monetary judgment in the *Rhodes* action." (App. 13a) To obtain such a judgment, Respondents had to commence a separate proceeding against Petitioners, which they did by bringing this case.

It was in this case that Petitioners were given a second opportunity to challenge Respondents' claims by submitting affidavits showing any facts which might make it inequitable to apply to them the rulings in *Rhodes* regarding the validity of the fee agreement. They submitted eight affidavits, all to no effect, because, as the court held,

> judging by the context of [Petitioners'] affidavits in the present action, their testimony in the *Rhodes* action, even assuming its veracity, would not have met the standard of professional conduct applied in the [*Rhodes*] case, having failed to allege, *inter alia*, that plaintiffs were informed their attorneys could be replaced without penalty.

(App. 69a; *see also* 7a) Thus, under the facts presented here, the Court of Appeals properly applied the equitable doctrine of collateral estoppel.

B. Petitioners Were Also Properly Bound By the Decision in *Rhodes* Because They Were in Privity with Rhodes

Petitioners also claim that the Court of Appeals erred by allegedly basing its determination that Petitioners were in "privity" with Rhodes solely on the "commonality of interest" they shared. Petitioners argue that the Court of Appeals

application of the doctrine of "privity" does not meet the constitutional standards of due process.

Petitioners misconstrue the Court of Appeals decision, which expressly stated that its determination of privity was based on "a confluence of factors . . . including [Petitioners'] relationship with Rhodes vis-à-vis the fee arrangements, their involvement in the action, their awareness of issues that would be decided, and their acknowledged tactical decisions regarding the *Rhodes* litigation." (App. 13a, n.*) In addition to these factors the Court of Appeals further emphasized that Petitioners were in privity with Rhodes because their rights derived from a single, indivisible fee arrangement Rhodes negotiated, as their law partner, on their collective behalf:

> [Petitioners] were in privity with their former law partner, Rhodes, . . . for purposes of litigating the validity of their fee arrangements as embodied in the trust . . . [because their] rights to receive payments were coextensive with Rhodes and derived from the identical arrangement entered into when the three were law partners. . . .

(App. 10a) Thus, Petitioners' relationship as "privies" of Rhodes was based on more than a shared interest in upholding the fee arrangement. They were partners at the time the fee arrangement was created,[11] their rights and obligations derived from that identical arrangement and, as the Appellate Division held, and Court of Appeals confirmed, their "right to receive trust income stands or falls with the contract." (*Id.*)

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11. As Rhodes' partners, Petitioners are liable for his misconduct in negotiating the illegal agreement, particularly since they were the beneficiaries of his misconduct. Under New Jersey law, where Petitioners and Rhodes were partners, "[i]t is fundamental that every member of a partnership is jointly and severally liable for torts committed by other members of the partnership acting within the scope of the firm business, even though they do not participate in, or ratify, or have knowledge of such negligence or legal malpractice." *Falzarano v. Leo*, 635 A.2d 547, 550 (N.J. Super. Ct. App. Div. 1993) (citing *Malanga v. Manufacturers Cas. Ins. Co.*, 146 A.2d 105 (N.J. 1958); N.J. Stat. Ann. § 42:1-15).

Richards, *supra*, and the other federal circuit precedent on which Petitioners rely, *Tice v. American Airlines, Inc.*, 162 F.3d 966 (7th Cir. 1998), *cert. denied*, 527 U.S. 1036 (1999), and *Becherer v. Merrill, Lynch, Pierce, Fenner & Smith, Inc.*, 193 F.3d 415 (6th Cir. 1999), have no bearing on this case. All of those cases concerned a "common-law kind of class action," *Tice*, 162 F.3d at 972, where a party was attempting to bind a broad class of litigants to a judgment in a prior action concerning a matter of public concern, even though the first action had not been brought on behalf of a class. Not surprisingly, the courts held that a mere commonality of interest with the litigants in the first action was not sufficient to meet the requirements of due process.

For instance, *Richards* involved two classes of taxpayers (the "*Richards* plaintiffs"), who sought to challenge the constitutionality of a county tax provision that had withstood a similar attack by three taxpayers in a prior litigation. This Court held that the *Richards* plaintiffs could not be precluded under the doctrine of *res judicata* because the *Richards* plaintiffs were "best described as mere 'strangers'" to the taxpayer litigants in the first action, they had not been given notice of that first action and the first action had not been brought on behalf of a class of taxpayers. 517 U.S. at 799-802.[12] Similarly, in *Tice*, the plaintiffs were American Airlines pilots, who were challenging certain of the airline's employment policies. The court held that they could

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12. *Richards* involved the broader doctrine of claim preclusion, which bars relitigation "not only of matters litigated and decided by it, but as to all relevant issues which could have been but were not raised and litigated in the suit." *Heiser v. Woodruff*, 327 U.S. 726, 735 (1946). In contrast, in this case, the Court of Appeals held that Petitioners were only precluded by the narrower doctrine of issue preclusion, which prevented them from relitigating only those precise issues that had been resolved in *Rhodes*. Thus, Petitioners were given the opportunity to – and did – assert affirmative defenses in this case that had not been asserted in *Rhodes*. However, the court held that Petitioners failed to raise an issue of material fact as to those defenses in response to Respondents' motion for summary judgment.

not be bound by prior litigation brought on behalf of other individual pilots, *not a class of pilots*, simply because they shared some, but not all, common interests. The court observed, that, unlike a "properly certified class action," the *Tice* plaintiffs did not have "adequate notice and (at a minimum) an opportunity to opt out of an earlier [litigation]." *Tice*, 162 F.3d at 972. *Becherer* raised a similar issue: whether a class of plaintiffs (the "Florida plaintiffs") could be bound by a judgment in a prior class action, despite that the Florida plaintiffs had only joined the class of plaintiffs in the first action as to certain discrete issues. The court held that it would violate Fed. R. Civ. P. 23 to bind the Florida plaintiffs on other issues that had not been certified as class issues simply because their "interests were identical" and they had a "'sufficiently close'" relationship to the class in the first action. *Becherer*, 193 F.3d at 419, 422.

The contrast between these cases and the present dispute is stark. Petitioners were not mere "strangers" to the *Rhodes* case with no notice of the matters being litigated and the potential effect of such litigation on their rights. They were parties on notice of the issues that were being litigated, they participated in the action, and they acknowledged to the court in New York the potential preclusive effect of a decision in *Rhodes* on their rights.[13] All of the factors required by the "normal privity analysis" are satisfied. *See Tice*, 162 F.3d at 973.

There is no reason to review the Court of Appeals decision with regard to collateral estoppel because Petitioners' right to due process was fully protected by the New York courts.

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13. Petitioners argue that there was no privity between them and Rhodes at the time of the trial in *Rhodes*, because their relationship with Rhodes had become "hostile and acrimonious by the time that Rhodes commenced the Rhodes action . . .". (Pet. 26, n.11) This notion of privity is far afield. At the time of the *Rhodes* trial, Rhodes and Petitioners were co-beneficiaries of a single trust agreement that reflected a single fee agreement negotiated in 1974 when they were partners. The validity of the fee agreement, and the lawyers' interest in the business trust, was a single issue that created privity.

CONCLUSION

For the reasons set forth above, the Petition for Writ of Certiorari should be denied.

Respectfully submitted,

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